

105TH CONGRESS
1ST SESSION

H. R. 420

To amend the Internal Revenue Code of 1986 to modify the exclusion of gain on certain small business stock and to allow nonrecognition on gain from the sale of such stock if other small business stock is purchased.

IN THE HOUSE OF REPRESENTATIVES

JANUARY 9, 1994

Mr. MATSUI (for himself and Mr. ENGLISH of Pennsylvania) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to modify the exclusion of gain on certain small business stock and to allow nonrecognition on gain from the sale of such stock if other small business stock is purchased.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE; AMENDMENT OF 1986 CODE.**

4 (a) SHORT TITLE.—This Act may be cited as the
5 “Enterprise Capital Formation Act of 1997”.

6 (b) AMENDMENT OF 1986 CODE.—Except as other-
7 wise expressly provided, whenever in this Act an amend-
8 ment or repeal is expressed in terms of an amendment

1 to, or repeal of, a section or other provision, the reference
2 shall be considered to be made to a section or other provi-
3 sion of the Internal Revenue Code of 1986.

4 **SEC. 2. FINDINGS.**

5 The Congress hereby finds that—

6 (1) investments in small business venture cap-
7 ital stock should be encouraged because of both the
8 special risks and the social and economic benefits as-
9 sociated with such investments,

10 (2) the exclusion from income of gain on small
11 business venture capital stock is an important incen-
12 tive for individuals and corporations to invest in
13 such stock, and

14 (3) tax incentives for investments in capital as-
15 sets in general should be supplemented with an ef-
16 fective tax incentive for investments in small busi-
17 ness venture capital stock.

18 **SEC. 3. MODIFICATIONS TO EXCLUSION OF GAIN ON CER-**
19 **TAIN SMALL BUSINESS STOCK.**

20 (a) INCREASE IN EXCLUSION PERCENTAGE.—

21 (1) IN GENERAL.—Subsection (a) of section
22 1202 is amended—

23 (A) by striking “50 percent” and inserting
24 “75 percent”, and

1 (B) by striking “50-PERCENT” in the
 2 heading and inserting “Partial”.

3 (2) CONFORMING AMENDMENTS.—

4 (A) The heading for section 1202 is
 5 amended by striking “**50-PERCENT**” and in-
 6 serting “**PARTIAL**”.

7 (B) The table of sections for part I of sub-
 8 chapter P of chapter 1 is amended by striking
 9 “50-percent” in the item relating to section
 10 1202 and inserting “Partial”.

11 (b) REDUCTION IN HOLDING PERIOD.—Subsection
 12 (a) of section 1202 is amended by striking “5 years” and
 13 inserting “3 years”.

14 (c) EXCLUSION AVAILABLE TO CORPORATIONS.—

15 (1) IN GENERAL.—Subsection (a) of section
 16 1202 is amended by striking “other than a corpora-
 17 tion”.

18 (2) TECHNICAL AMENDMENT.—Subsection (c)
 19 of section 1202 is amended by adding at the end the
 20 following new paragraph:

21 “(4) STOCK HELD AMONG MEMBERS OF CON-
 22 TROLLED GROUP NOT ELIGIBLE.—Stock of a mem-
 23 ber of a parent-subsidiary controlled group (as de-
 24 fined in subsection (d)(3)) shall not be treated as

1 qualified small business stock while held by another
 2 member of such group.”.

3 (d) REPEAL OF MINIMUM TAX PREFERENCE.—

4 (1) IN GENERAL.—Subsection (a) of section 57
 5 is amended by striking paragraph (7).

6 (2) TECHNICAL AMENDMENT.—Subclause (II)
 7 of section 53(d)(1)(B)(ii) is amended by striking “,
 8 (5), and (7)” and inserting “and (5)”.

9 (e) STOCK OF LARGER BUSINESSES ELIGIBLE FOR
 10 EXCLUSION.—

11 (1) Paragraph (1) of section 1202(d) is amend-
 12 ed by striking “\$50,000,000” each place it appears
 13 and inserting “\$100,000,000”.

14 (2) Subsection (d) of section 1202 is amended
 15 by adding at the end the following new paragraph:

16 “(4) INFLATION ADJUSTMENT OF ASSET LIM-
 17 ITATION.—In the case of stock issued in any calendar
 18 year after 1997, the \$100,000,000 amount con-
 19 tained in paragraph (1) shall be increased by an
 20 amount equal to—

21 “(A) such dollar amount, multiplied by

22 “(B) the cost-of-living adjustment deter-
 23 mined under section 1(f)(3) for the calendar
 24 year in which the taxable year begins, deter-
 25 mined by substituting ‘calendar year 1996’ for

1 ‘calendar year 1992’ in subparagraph (B)
2 thereof.

3 If any amount as adjusted under the preceding sen-
4 tence is not a multiple of \$10,000, such amount
5 shall be rounded to the nearest multiple of
6 \$10,000.”.

7 (f) REPEAL OF PER-ISSUER LIMITATION.—Section
8 1202 is amended by striking subsection (b).

9 (g) OTHER MODIFICATIONS.—

10 (1) REPEAL OF WORKING CAPITAL LIMITA-
11 TION.—Paragraph (6) of section 1202(e) is amend-
12 ed—

13 (A) by striking “2 years” in subparagraph
14 (B) and inserting “5 years”, and
15 (B) by striking the last sentence.

16 (2) EXCEPTION FROM REDEMPTION RULES
17 WHERE BUSINESS PURPOSE.—Paragraph (3) of sec-
18 tion 1202(c) is amended by adding at the end the
19 following new subparagraph:

20 “(D) WAIVER WHERE BUSINESS PUR-
21 POSE.—A purchase of stock by the issuing cor-
22 poration shall be disregarded for purposes of
23 subparagraph (B) if the issuing corporation es-
24 tablishes that there was a business purpose for
25 such purchase and one of the principal purposes

1 of the purchase was not to avoid the limitations
 2 of this section.”.

3 (h) QUALIFIED TRADE OR BUSINESS.—Section
 4 1202(e)(3) is amended by inserting “and” at the end of
 5 subparagraph (C), by striking “, and” at the end of sub-
 6 paragraph (D) and inserting a period, and by striking sub-
 7 paragraph (E).

8 (i) EFFECTIVE DATES.—

9 (1) IN GENERAL.—Except as provided in para-
 10 graph (2), the amendments made by this section
 11 shall apply to stock issued after August 10, 1993.

12 (2) SPECIAL RULE.—The amendments made by
 13 subsections (b), (c), and (e) shall apply to stock is-
 14 sued after the date of the enactment of this Act.

15 (j) ELECTION TO APPLY AMENDMENTS TO STOCK
 16 ISSUED AFTER AUGUST 10, 1993.—

17 (1) IN GENERAL.—The amendments made by
 18 subsections (b), (c), and (e) shall apply to any quali-
 19 fied stock issued after August 10, 1993, if the tax-
 20 payer elects to apply such amendments with respect
 21 to such stock.

22 (2) QUALIFIED STOCK.—For purposes of para-
 23 graph (1), the term “qualified stock” means stock—

24 (A) which is held by the taxpayer on the
 25 date of the enactment of this Act, and

(B) which was not qualified small business stock (as defined section 1202(c) of the Internal Revenue Code of 1986) when issued but which would be qualified small business stock (as so defined) if the amendments made by subsections (b), (c), and (e) applied to stock issued after August 10, 1993.

(3) RECOGNITION OF GAIN.—For purposes of the Internal Revenue Code of 1986—

(A) IN GENERAL.—Any qualified stock to which the election under paragraph (1) applies shall be treated—

(i) as having been sold on the date of the enactment of this Act for an amount equal to its fair market value on such date, and

(ii) as having been reacquired on such date for an amount equal to such fair market value.

The preceding sentence shall not apply for purposes of determining whether the stock is qualified small business stock (as so defined).

(B) TREATMENT OF GAIN OR LOSS.—

(i) Any gain resulting from subparagraph (A) shall be treated as received or

1 accrued on the date of the enactment of
 2 this Act, and shall be recognized notwith-
 3 standing any provision of the Internal Rev-
 4 enue Code of 1986.

5 (ii) Any loss resulting from subpara-
 6 graph (A) shall not be allowed for any tax-
 7 able year.

8 (4) ELECTION.—An election under paragraph
 9 (1) shall be made in such manner as the Secretary
 10 may prescribe and shall specify the stock for which
 11 such election is made. Such an election, once made
 12 with respect to any stock, shall be irrevocable.

13 **SEC. 4. ROLLOVER OF GAIN FROM SALE OF QUALIFIED**
 14 **STOCK.**

15 (a) IN GENERAL.—Part III of subchapter O of chap-
 16 ter 1 is amended by adding at the end the following new
 17 section:

18 **“SEC. 1045. ROLLOVER OF GAIN FROM QUALIFIED SMALL**
 19 **BUSINESS STOCK TO ANOTHER QUALIFIED**
 20 **SMALL BUSINESS STOCK.**

21 “(a) NONRECOGNITION OF GAIN.—In the case of any
 22 sale of qualified small business stock with respect to which
 23 the taxpayer elects the application of this section, eligible
 24 gain from such sale shall be recognized only to the extent
 25 that the amount realized on such sale exceeds—

1 “(1) the cost of any qualified small business
2 stock purchased by the taxpayer during the 60-day
3 period beginning on the date of such sale, reduced
4 by

5 “(2) any portion of such cost previously taken
6 into account under this section.

7 This section shall not apply to any gain which is treated
8 as ordinary income for purposes of this title.

9 “(b) DEFINITIONS AND SPECIAL RULES.—For pur-
10 poses of this section—

11 “(1) QUALIFIED SMALL BUSINESS STOCK.—The
12 term ‘qualified small business stock’ has the mean-
13 ing given such term by section 1202(c).

14 “(2) ELIGIBLE GAIN.—The term ‘eligible gain’
15 means any gain from the sale or exchange of quali-
16 fied small business stock held for more than 3 years.

17 “(3) PURCHASE.—A taxpayer shall be treated
18 as having purchased any property if, but for para-
19 graph (4), the unadjusted basis of such property in
20 the hands of the taxpayer would be its cost (within
21 the meaning of section 1012).”

22 “(4) BASIS ADJUSTMENTS.—If gain from any
23 sale is not recognized by reason of subsection (a),
24 such gain shall be applied to reduce (in the order ac-
25 quired) the basis for determining gain or loss of any

1 qualified small business stock which is purchased by
 2 the taxpayer during the 60-day period described in
 3 subsection (a).

4 “(c) SPECIAL RULES FOR TREATMENT OF REPLACE-
 5 MENT STOCK.—

6 “(1) HOLDING PERIOD FOR ACCRUED GAIN.—

7 For purposes of this chapter, gain from the disposi-
 8 tion of any replacement qualified small business
 9 stock shall be treated as gain from the sale or ex-
 10 change of qualified small business stock held more
 11 than 3 years to the extent that the amount of such
 12 gain does not exceed the amount of the reduction in
 13 the basis of such stock by reason of subsection
 14 (b)(4).

15 “(2) TACKING OF HOLDING PERIOD FOR PUR-
 16 POSES OF DEFERRAL.—Solely for purposes of apply-
 17 ing this section, if any replacement qualified small
 18 business stock is disposed of before the taxpayer has
 19 held such stock for more than 3 years, gain from
 20 such stock shall be treated eligible gain for purposes
 21 of subsection (a).

22 “(3) REPLACEMENT QUALIFIED SMALL BUSI-
 23 NESS STOCK.—For purposes of this subsection, the
 24 term ‘replacement qualified small business stock’

1 means any qualified small business stock the basis
2 of which was reduced under subsection (b)(4).”.

3 (b) CONFORMING AMENDMENTS.—

4 (1) Section 1016(a)(23) is amended—

5 (A) by striking “or 1044” and inserting “,
6 1044, or 1045”, and

7 (B) by striking “or 1044(d)” and inserting
8 “, 1044(d), or 1045(b)(4)”.

9 (2) The table of sections for part III of sub-
10 chapter O of chapter 1 is amended by adding at the
11 end the following new item:

“Sec. 1045. Rollover of gain from qualified small business stock
to another qualified small business stock.”.

12 (c) EFFECTIVE DATE.—The amendments made by
13 this section shall apply to stock sold or exchanged after
14 the date of the enactment of this Act.

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